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Economic Conditions
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General Business Conditions

THE year 1935 is opening with business activity on a slightly higher scale than at the beginning of 1934, and probably most American business men expect that the year as a whole will be better than 1934, even though many of the unfavorable conditions which have hampered progress are still persisting. The turn for the better in trade and industry during the past two or three months has had a plainly heartening effect upon expectations for 1935. To be sure, business sentiment naturally improves when trade improves, and as readily declines when trade declines; and the fact that sentiment is better is no assurance as to how long the trade improvement will last. However, the upward trend has been gaining momentum; and on the basis of orders on hand in some industries, seasonal prospects in others, and the reduction of merchandise stocks due to good Christmas trade, it seems likely to extend at least into Spring.

Christmas trade, according to preliminary reports, has run all the way from 5 to 10 per cent better than last year, in the Eastern industrial centers, to 20 or 30 per cent higher in some agricultural districts, notably in the South and Southwest. With prices about the same, the gains are due in part to greater volume, and partly to purchases of more expensive goods. After these gains wholesale trade in January is expected to be satisfactory.

Along with the trade improvement industrial production has made a better than seasonal showing. The rise in steel mill operations, which has been under way for ten weeks, was not broken even by the holidays. An insistent demand for steel deliveries has come from the automobile manufacturers, who are rapidly expanding assemblies of their new models, after a satisfactory cleanup of dealers' stocks of 1934 cars. It had been feared that cotton mills would curtail very sharply over Christmas, but they made unusual sales gains during December, and operations have held up better than expected. Other branches of the textile industry are giving more support to business than since last Spring, and have a better backlog of orders than a year ago. Reports from other industries also indicate that general business indexes for December, when final figures are assembled, will show the best gain in nearly a year.

Importance of the Capital Goods Industries

The chief question as to the outlook for the latter part of 1935 is whether the improvement described will spread to the machinery, construction, and other capital goods industries. Wear and tear and replacement of goods of every day use have brought other upswings in the industries making such goods, but they have not led to recovery. Unless the improvement extends to the capital goods industries, and thus leads to a balanced recovery embracing all elements of the economic system, it will exhaust itself, and activity will lapse again.

The conditions which affect the demand for capital goods are incomparably more complex than those which affect the demand for consumer goods, especially at a time when the relief expenditures of the Government are helping to make up the deficit in consumers' buying power. If the industries are to spend for new productive equipment they must first feel assurance that they can make it pay for itself, which requires that the goods produced must be salable at a profit. The price of the equipment must be in equitable relation to other prices, and to the ability to pay. Since equipment is bought to use for several years the buyers must have confidence in the stability of the economic situation so far as they can see ahead, and must have the incentive of profit to accept the risks of developments that they cannot foresee. They must have either money or credit, and if they find it necessary to raise capital or borrow to carry out their projects, as is usually the case where large sums are required, the lender or investor enters the picture. He must be satisfied not only of the correctness of the borrower's judgment of the

situation, but must feel additionally an assurance that the money repaid to him will be of the same value as the money he lends.

Only in the degree that the business situation makes progress toward satisfying these requirements can it be considered improving. They are offered as broad tests for determining in which respects the economic situation was bettered during 1934, and in which it deteriorated. Government expenditures, also a factor in business, are outside the natural economic influences. They can give the consumer goods industries support, as long as they can be continued, but their stimulus is largely counteracted, by the distrust which they inspire, before it reaches the capital goods group.

1934 Developments—Better Price Relationships

The chief requirement for the free production and consumption of goods of every day use is that they can be priced, allowing for costs and profit, to accord with the ability of consumers to pay. Unquestionably a principal cause of the disruption of trade has been the disparity that developed between the prices of finished goods and those of raw materials, among which the farm products are most important, in view of the extent of the farm market. Until the drouth became a factor on the farm side little progress was made toward overcoming this disparity, the N.R.A. raising goods prices as fast as the A.A.A. raised farm prices. But since last Spring the spread has been closing rapidly. Retail merchandise prices in December have been slightly lower than a year ago, and retail food prices are only 8.6 per cent higher. But farm prices are up 25 per cent. On November 15 the ratio of farm prices received to prices paid was 81 per cent of the pre-war average, against 69 per cent one year earlier. This ratio takes no account of the rental and benefit payments from the A.A.A.

This is a genuine gain. It has given the farmer, despite the crop disaster, the largest cash income since 1931, and made him a correspondingly important factor in trade. It is a reasonable assumption that the improvement will hold through 1935, for the drouth has removed the surplus supplies that were depressing the markets, average crops will not be a threat to the farm price level, and if larger crops are grown and sold at present prices the farm income in 1935 will be even larger.

Moreover, there are reasons, aside from the showing of the indexes, for believing that the rise in finished prices which began under the N.R.A. is checked, except as further rises in raw materials may advance them. The suspension within the past month of the price-fixing provisions of the lumber code is another sign that the policy of the overhead authority is toward gradually restoring price competition in industries where it has been abridged. Support for proposals such as the 30-hour week which would sharply increase costs seems to be diminishing, Mr. Richberg being among those who have stated the dangers of too rapid increases in wage costs. All this implies a check to arbitrary cost increases, and more freedom for the efficient producers to pass on the benefits of their efficiency, without having to conform to regulations protecting their less able or less favorably situated competitors. Also, the situation is certain to stimulate cost reductions, permitting price reductions.

Thus from both sides the raw material-retail price spread is narrowed. This is a fundamental improvement in economic relationships, facilitating trade. To be sure the comparison would be unfavorable if made with pre-depression figures, due to the rise in costs in 1933, and it leaves out of account all consumers who have had no increases in income in the past eighteen months, or a smaller increase than the retail price rise. But in 1934 at any rate the trend has been in the right direction, and the gain in merchandise sales this Fall demonstrates the benefits.

Improvement in Earnings

Another respect in which progress has been made during 1934 is in the restoration of the manufacturing industries to an earnings basis. This statement is very seriously qualified by the fact that third quarter earnings, for the reports available, were 35 per cent less than in the same period of 1933, and that the fourth quarter showing is uncertain. However, the first six months showed a gain, and with that start the year's operations will probably yield capital a small return. In 1933 the manufacturing industries barely broke even, and in 1932 and 1931 they operated at a loss.

This improvement will be attacked by some persons who believe that profits are an unfair tribute exacted from labor and the consumer and contributing to a maldistribution of wealth, but this is a complete and harmful misconception. We have discussed the nature and extent of profits in recent issues of this Letter, and do so elsewhere in this issue, and cannot repeat the discussion here. But it is necessary to emphasize that the establishment of a normal profit, and provision for it in prices, does not endanger the restoration of the business equilibrium, nor act as an obstacle to recovery. In truth profits serve exactly to the contrary. They constitute purchasing power as truly as the income of the laborer or farmer constitutes purchasing power, with the addition that the purchasing power retained by the industries is employed for a special use, to wit, the purchase of industrial or capital goods. This is the area in which purchasing power is lacking, and in

which depression is greatest. It is the area in which improvement is most urgently needed to effect a balanced recovery.

In short, profits are the very agency by which recovery will come. They are necessary if business men are to be encouraged to go ahead and spend on equipment, and if the industries are to be entitled to the credit and the new capital which everyone desires to see them use. Undoubtedly profits in 1935 will be affected chiefly by the volume of business over which costs must be distributed, and the present uptrend in volume is hopeful. It is reasonable to expect that if the industries can make money in the forepart of 1935, bringing them two full years away from deficit operations, their expenditures on maintenance, replacements and new projects will increase. Present schedules for such expenditures, while moderate, show some expansion.

The Financial Situation

The third area in which 1934 developments have been favorable for business recovery is in certain aspects of the financial situation. There is no further concern for the safety of the banks, and the trend away from further monetary experimentation has been marked. The silver buying policy is not being pushed vigorously. The dollar has been tied to its new gold value for eleven months, although business has been so depressed during part of that period that a case for another devaluation might readily have been presented if there were belief that it would promote recovery. Hence the situation inspires confidence that a new devaluation is not intended, and this confidence has helped the bond market. Corporate bond prices have advanced 15 to 20 per cent on the average during the year, and high-grade bonds have reached levels unequalled within the experience of present day business men; this despite the absorption of an unparalleled proportion of the country's investment funds into the Government bond market.

This advance is evidence that on the side of the supply of funds, and the willingness to employ them where security of principal can be found, there is no obstacle to revival in the capital markets. Also, the inducement to assume an increased risk by extending investments into the lower-rated bonds is greater than heretofore, and it is the observation of many experienced bond men that the willingness to "reach down" is spreading. This tendency if continued will lead to an increase in new industrial financing. Already the bond market improvement has simplified the problem of refinancing. It is permitting the retirement of high-coupon bonds by borrowing at lower rates, thus reducing overhead costs, and it is relieving the anxieties of corporation executives as to their ability to meet maturities, which may increase their disposition to spend upon plant improvement funds held for that purpose.

The paying off of old debts or readjustment of them to a new basis has proceeded to such good effect that values are more stable in quarters where selling to pay debts has been pronounced. A good many mortgage situations have been cleared up and distressed properties have been absorbed. Prices of farm land have turned upward, and rents and prices of residential property also to some extent. These are signs accepted by experience as marking the turn in a depression. Of course account should be taken of the Government support given to the mortgage situation.

Gains in the foreign exchange situation may also be referred to, though unfortunately the outlook is not everywhere clear. Within the past month Mr. Neville Chamberlain, the British Chancellor of the Exchequer, has indicated the unlikelihood of an early return of the pound to gold. However, the pound has been more stable, and the wide fluctuations in many currencies characteristic of 1933, and disruptive of trade, have been fewer. Many of the important raw material producing countries, such as Argentina and Brazil, have been able to modify their restrictions on the transfer of funds to other countries, and the ability to trade with them is increased accordingly. Our exports, except in agricultural products, have increased considerably during 1934, in both quantity and value, and this is due to improved conditions in other countries as well as to the temporary advantage obtained by our exporters from the devalued dollar.

Elements of Uncertainty

The developments described constitute the chief economic gains during 1934. They are starts in the right direction, along the road most favorable for natural business improvement. Of course they are but a few of the elements in the economic situation, and it is evident from the state of business that there are other weighty influences which are pulling the opposite way. Last year was the fifth year of the depression, and as it has dragged on the resources of individuals have been cumulatively exhausted. Hence the relief rolls are longer than ever before, including almost 19,000,000 persons, and three-quarters of the relief burden is falling on the Federal Treasury. Likewise the position of some industries least benefitted by the improvement has shown further deterioration. The railways for the third successive year have had a deficit after interest charges, and a greater one than in 1933. The curtailment of railway expenditures for replacements and improvements is a very important element in the depression. The

roads need the improvements as much as the equipment business needs the orders, but obviously deficits limit capital expenditures. Also, little headway is being made toward making the roads self-supporting.

The latest building figures do not make a good showing. Contract awards in the first three-quarters of December, reduced to a daily average, were 22 per cent less than in November, which is more than the usual seasonal decline, and 56 per cent below a year ago. Looking ahead to Spring, the building industry is optimistic, and the efforts being made to revive it are impressive, although it could be wished that they included a greater emphasis on reducing costs.

It is recognized that the effects upon trade of the favorable factors described will be supplemented by the heavy Government expenditures to be made during 1935, but even those whose business benefits from these expenditures view them with concern. Unquestionably the taxpayers of this country are ready to accept the burden of relief and of any other expenditure that will get business out of the depression and the unemployed back to work, but as a practical people they expect to get value received for what they spend, and the continuous unemployment and mounting relief rolls do not inspire confidence that the program is operating as intended. Everyone realizes that there is a limit, not precisely determinable to be sure, to Government expenditures, and naturally there are apprehensions as to what the situation will be when the limit is reached, unless meanwhile the economic system is restored to a self-supporting basis.

This may fairly be described as the dilemma of the recovery program. Government expenditures are intended to bridge the gap until private enterprise will take hold and the people support themselves; yet Government expenditures discourage private enterprise.

What solution can be found for this dilemma? Surely there is none but to work upon it from both ends: on the one hand, to establish control of Government expenditures by a rigorous limitation to necessary relief payments, and to such projects as will be self-supporting and will not result in unnecessary duplication of productive facilities and hence discourage private enterprise; and on the other, to facilitate, both through the policies of the Government and the cooperation of the members of the economic system, which includes everyone, the restoration of self-supporting industry.

The Question of Business Regulation

Part of the recovery program has been an attempt to restore the equilibrium in the economic system by the exercise of overhead authority and detailed regulation of business. However, the attempt has been based upon the judgment of the overhead authority as to the respects in which the system was out of balance, rather than upon the automatic judgments of the system itself, and the arbitrary judgments do not appear to have been superior. After eighteen months' experience the policy is toward relaxing the detailed regulation of business, in order to give greater scope to the self-balancing character of the system.

It is worthy of note that all the efforts of the overhead authorities, taken together, have been less effective in balancing the economic system than the drouth, which by removing the agricultural surpluses has brought farm prices into the fairer relationship with industrial prices that has already been described. To be sure this is establishing equilibrium on a basis of scarcity and high prices rather than plenty and low prices. The industrial controls themselves have tended to impair the equilibrium by raising costs more rapidly than purchasing power could increase. They have pegged costs and prices which are out of line with other costs and prices. They have, in the long run, diminished the expectation of profits, and by dealing with the efficient exactly as with the inefficient they have lessened the value of initiative and enterprise. They have tended to force business into a set pattern, to impair the flexibility with which the industries could adjust prices and costs, and thus have reduced the ability of the economic system to find its own balance.

The experiment with overhead control was brought about by the calamitous experience of the depression, and all elements of the population have given their support. Those who have administered the control have made a vigorous and sincere effort to reestablish the equilibrium, and the American people have been persuaded by their hardships to accept supervision and regimentation to a degree which heretofore would have been considered utterly impracticable. Hence the trial has been a fair one. However, President Roosevelt was moved to inquire, in his most recent radio speech, whether certain of the policies have been "best calculated to promote industrial recovery and a permanent improvement of business and labor conditions"; and he assumed leadership in modifying the controls.

There is reason to think that gradual modifications of the regulation will be generally welcomed. Other things being equal, the American people prefer to be free of restraint, and to submit themselves to overhead authority only as long as its superiority to natural forces is evident and its benefits indubitably demonstrated.

Probably the most significant fact in the outlook for 1935 is that the decisions to be

taken by governmental bodies may dominate the economic situation. These decisions are incalculable. Insofar as the calculable economic influences may control, there is warrant, in the gains described, for the present hopefulness.

Money and Banking

The conditions of extreme ease, long prevalent in the money market, remained undisturbed during December, despite seasonal currency demands and customary year-end window dressing for financial statements. Holiday currency expansion, as a matter of fact, was rather less than usual, despite the generally good reports of retail trade, the explanation possibly being a greater use by shoppers of currency previously hoarded. While December revenue collections likewise took funds temporarily out of the market, these losses were counterbalanced by gold imports amounting to $85,000,000, so that bank reserves dipped only moderately, and excess reserves remained above $500,000,000 for New York City banks alone and around $1,700,000,000 for all member banks.

Open market rates for Stock Exchange money, commercial paper and acceptances were unchanged; nevertheless, an easier trend of money was visible in a reduction in the average discount basis for new 6-months Treasury bills to 0.12 per cent, compared with 0.29 in the last week of September and 0.07 at the July low point. Indicative also of the tendency of interest rates was the action of the Federal Reserve Banks of Atlanta and Kansas City in cutting their rediscount rates from 3 to 2½; the action of the Federal Reserve Board and Federal Deposit Insurance Corporation in ordering reductions from 3 to 2½ per cent in the maximum rates paid by member institutions on time and savings deposits; and the action of two leading insurance companies in announcing a new rate of interest for computing premiums and reserves at 3 per cent, instead of 3½ per cent as heretofore.

The Expansion of Bank Credit

Government operations were a large factor in the money market during the month, the sale of new Treasury issues on the 15th being accompanied by a further substantial expansion of bank credit. During the week of the 15th, the holdings of Government securities by the weekly reporting banks increased by $367,000,000, and Government deposits by $572,000,000, the latter figure raising Government balances in the banks to $1,343,000,000, the highest since last July. As these balances are drawn upon by the Treasury in payment of its bills, further increases in demand deposits of the banks over the next few months are to be anticipated.

A comparison of the current position of these banks with that of a year ago reveals increases of $3,358,000,000 and $1,645,000,000 in deposits and aggregate loans and investments, respectively, a by no means insignificant growth in bank credit in a year's time.

This expansion, however, has been largely the result of Government, rather than of private borrowing, all, and more, of the total increase in loans and investments being accounted for by the increase in bank holdings of Government securities ($1,888,000,000). While holdings of other investment securities also increased, loans declined by $714,000,000, reflecting principally a liquidation of loans on securities, and some reduction in unsecured loans, often considered roughly indicative of commercial borrowing.

The fact that unsecured loans have decreased over the past year is attributable mainly to the generally light demand for credit on the part of bank customers in good standing. In addition, the heavy disbursements by the Government have facilitated the liquidation of old slow loans, thus tending to offset the current lending activities of the banks.

The Bond Market

The December 15th Treasury financing included retirement of $992,000,000 of maturing 2¼ per cent one-year certificates, and the issuance of $976,000,000 of 1⅛ per cent 18-months notes and 2⅛ per cent for 4½-year notes in exchange thereof. In addition, the Treasury sold for cash $476,000,000 of the 1⅛ per cent notes and $491,000,000 of 3⅛ per cent 13-16-year bonds. The favorable response to the offering of long-term bonds was particularly gratifying to the Treasury, inasmuch as the floating debt, consisting of Treasury bills, certificate and note issues and the Fourth Liberty loan, all due within five years and requiring frequent renewal, now comprises more than half of the gross debt. Subscriptions to the long-term bonds totalled $2,330,469,500, or more than five times the amount of the offering, and the bonds are now selling at a premium of more than a point over par.

Outstanding bonds reflected the heavy oversubscription to the new Treasury offerings and the downward trend of interest rates, with prices of Governments, municipal and high-grade corporate issues making further gains. Numerous issues established new high records in December, and the Standard Statistics Company's index of yield on municipal bonds reached 3.49 per cent, which is the lowest average yield recorded by this index since 1906.

The reviving trend in volume of new financing was continued last month, when a number of important municipal and corporate issues were sold. A feature of the offerings was an

issue of $40,000,000 of serial 3¾ and 4 per cent bonds of the City of New York, which was readily absorbed by the market. These bonds were purchased by a banking syndicate at an interest rate to the City of 3.98 per cent, and were reoffered to the public at prices yielding returns ranging from 2 to 4 per cent, depending on maturities.

The Monetary Crisis in China

In the November issue of this Letter we described at length the effects of the United States Government's silver purchase program upon China and the efforts of the Chinese Government to protect the country's monetary system by the imposition of a tax and equalization fee upon exports of silver. Since that time the economic difficulties of China have become steadily worse. With silver worth substantially more outside of China than inside, it has been impossible to prevent smuggling on a large scale, partly nullifying the effects of the embargo. Moreover, the Chinese people have felt a growing lack of confidence in the effectiveness of the measures taken to prevent the country's circulating medium from being drained off to the United States, and have been disposed to convert their currency and bank deposits into hard cash which they can put away. In this respect the situation is similar to that which developed in the United States early in 1933 when everyone was trying to get gold.

In consequence of the loss of silver through exports, transfers to the interior and public hoarding of cash, the visible stocks of silver in Shanghai have been undergoing a steady shrinkage, as revealed by the following table:

Shanghai Silver Stocks (in ounces)

1934, May	447,280,000
" June	446,220,000
" July	426,420,000
" August	381,840,000
" September	348,460,000
" October	321,360,000
" November	283,000,000
" December (15)	267,000,000

At least until the end of October this reduction of the silver stocks apparently caused no general alarm, inasmuch as the note issues of the Shanghai banks at that date—the latest for which figures are available here—were still showing an increase. By the latter part of November, however, cable advices gave evidence of growing tension. With the drain on silver stocks apparently continuing, the situation during December has been one of acute strain. Money has been so tight that rates up to 20 per cent have been paid for short accommodation. The pressure on the banks has been severe, and two small Chinese banks are reported to have failed, one with a capitalization of $500,000.

Production Hit by Silver Advance

Aside from the banking crisis caused by the drain on specie reserves, the situation in China is complicated by the deflationary effect of the rise in the value of silver on Chinese trade. This appreciation in the value of Chinese money is having the same effects upon the Chinese economy that a similar rise in the dollar or the pound would have in the United States or Great Britain. It facilitates imports and discourages exports, thus forcing down the price level, with all the attendant evils of business losses and unemployment. During the period while the price of silver was falling, China was saved from the effects of the deflation of general prices and depression of trade existing in other countries. Since silver began rising, however, prices in China have been declining, excepting only a few months in the Summer of this year when the rise of prices of certain agricultural products, caused by short crops, was great enough to offset the rise of silver. Reflecting the effects of higher silver prices,—which are said to have encouraged foreign competition, particularly Japanese,—and also the banking crisis, production in China is reported to have been hard hit lately, the New York Times correspondent cabling on December 15 that decreases within a month include: weaving and spinning, 25 per cent; hatmaking, 30; silk filatures, 80; dyestuffs, 40; printing, 45; painting, 40; electric appliances, 45; ironworks and glassware, 50; and rubber goods, 35 per cent.

Chinese Balance of Payments Unfavorable

An additional difficulty in connection with the Chinese situation lies in the fact that the balance of payments, normally favorable to China, has been unfavorable since 1931, necessitating the shipment of silver by way of settlement. Undoubtedly a principal cause of this shift in China's position has been the depreciation of the pound sterling and Japanese yen, which has tended to make foreign goods relatively cheaper than Chinese; also, the reduction of the usual flow of emigrant remittances, in consequence of the depression, has been an important factor in the situation. With the situation already in disequilibrium, and conducive to silver exports, the further pushing up of silver prices has served to accentuate this maladjustment by making Chinese goods still dearer in terms of competing currencies.

In other words, the silver purchase plan of the United States not only affects the Chinese currency system directly, by encouraging the withdrawal of Chinese silver money for conversion into bullion and sale to the United States Treasury, but indirectly, by raising the value of the Chinese currency and so affecting the balance of payments that silver has to be exported to cover the deficiencies.

U. S. Silver Program Hurtful to Trade With China

Evidently, there is something wrong with the arguments of the silver party in this country to the effect that a rise in the price of silver would increase the purchasing power of China and so contribute to an expansion of world trade in which the United States would participate. As a matter of fact, if the price of silver continues to rise the outcome seems more likely to be a smaller rather than a larger American trade in the Orient. Already the difficulties into which China has been plunged have forced that country to the adoption of some measures and consideration of others which may affect our trade adversely in that quarter. The imposition of an export tax on silver is in effect an abandonment by China of the silver standard, at least in international relations, and the adoption in its place of a managed currency. With the Chinese currency no longer tied to metal, there is no certainty to what lengths of depreciation it might go, particularly if the drain of metal from the country continues. Several years ago when Chinese exchange was falling with the price of silver, there was a great outcry against "destructive Chinese competition", and it is no secret that some of the advocates of raising the price of silver have had in mind not so much increasing the purchasing power of China as putting an end to this exchange competition by raising the value of her currency. It ought to have been recognized that one country cannot manipulate another's currency against the latter's will. All that China had to do was to cut loose from silver, which she has done. Once afloat on the sea of managed currency there is no telling what the destination may be, and whether we may not eventually find ourselves facing a new competition fully as "destructive" as the last.

A natural consequence also of China's exchange difficulties has been to give impetus to nationalist sentiment and to promote measures calculated to make the country more self-sufficient as to imports. At a meeting held in December, the Central Executive Committee of the Kuomintang (Nationalist party) went on record in favor of higher import duties, and even adopted a resolution urging the Nationalist Government to establish an automobile factory as part of a domestic industrial expansion program. At the same time, it is reported that public opinion is running very high against the United States which is considered to be pursuing a course inimical to China. Clearly, these developments do not give promise of much enlargement of our trade in that part of the world.

The Question of the "Right" of the United States to Do as It Pleases

Perhaps it may be said that the United States has a right to enact any monetary legislation which it considers to be in its interest, regardless of the effect upon other nations. No one, of course, denies this, and the Chinese Government, in its notes of protest to our Government, has not questioned the "right" of the United States to accumulate silver if it wishes to do so. That no country, however, can afford to ignore the consequences of its acts and policies upon other countries would seem to be self-evident. The United States Government itself has widely proclaimed the "good neighbor" policy as the basis of its foreign diplomacy, which implies a recognition of the interests of other countries. Certainly, a callous disregard of the interests of China in connection with silver would not be in accord with this policy.

Moreover, in view of the terms and purposes of the London Agreement on silver, to which China and the United States were both signatories, the question may be raised as to whether the United States is dealing fairly with China in pursuing a course so clearly antagonistic to the latter's interest. The basis of that agreement was that all nations should cooperate in the measures taken to rehabilitate silver. It was stated clearly in the text that "agreement be sought . . . *with a view to mitigating the fluctuations in the price of silver*", and it was on that basis that China's signature was affixed. Furthermore, it will be recalled that President Roosevelt, in his proclamation of December 21, 1933, ratifying the London Silver Agreement, declared it to be one of the purposes of his action to "augment the purchasing power of peoples in silver-using countries." In the light of these solemn pledges, what now is to be said of a program which is creating new and still more disturbing fluctuations in silver prices and spreading unemployment and distress in one of the chief countries still using silver as money?

Quite apart, however, from questions of ethics, it should still be clear that the United States cannot afford to be indifferent to the consequences of its acts in the Far East. The United States is interested in the stability of exchanges and in free channels of trade in China and other eastern countries. Yet, actually, its policy with respect to silver seems more calculated to bring about conditions just the reverse of this. What appears to threaten are more trade barriers and more exchange wars,—in short, more of the same complications which have been responsible for the general state of disorder existing all over the world and which have been holding back recovery.

The Problem of a Remedy

The American Secretary of State has responded to the protests of the Chinese Gov-

ernment that this Government desires to avoid so far as may be possible disturbances to the economy and public finance of China. The difficulty is that the silver purchase program is embodied in an act of Congress which is mandatory, as to its general objective, though the President is given discretionary powers as to time, rapidity of accumulation and prices.

The suggestion has been made that the United States might relieve the situation at least temporarily by extending a silver loan to the Chinese Government. It is difficult, however, to see how this would afford any permanent solution. The United States would be buying silver from China with one hand and lending it back to her with the other, merely postponing the day of reckoning, and in the meantime getting the Chinese people more deeply in debt.

It has been suggested also that China might devalue her currency, but in this likewise it is difficult to see any final remedy. It must be borne in mind that the bulk of China's silver is in the hands of the public, and that the problem, therefore, of revaluing the currency is quite different from what it was in the United States where the metallic reserves were held largely by the Government and the central bank. Moreover, if the United States continues its buying program what reason is there to believe that one revaluation will not simply lead to another?

In short, no means of defense open to China seems likely to be effective in the face of continued aggressive bidding for silver by the United States Government. With every rise in the price of silver, and increase in the disparity between Chinese exchange and the world price of silver, the incentive to smuggling will be increased. The danger, then, would be in further heavy drains on the monetary supplies of the country, leading sooner or later to runs on the banks, hoarding and general financial collapse. Were the United States Government willing to modify its program sufficiently to prevent a further widening of the exchange spread, it is possible that China might be able to work out methods of controlling the situation. The power to do this is well within the authority of the Executive, and does not imply a nullification of the will of Congress. The Treasury need simply limit its purchases to the silver offered around current prices, without further bidding up of the market, in which case it is quite probable that the actual volume of silver acquired would be greater than the Treasury is now getting, as speculators would be discouraged from holding for a larger profit. In following this policy, this Government would be lessening the danger of further serious trouble in the Far East by removing what is perhaps the chief cause of alarm in China, to wit, uncertainty as to how far the United States Government intends to go in forcing up the price of silver.

France to Drop Wheat Price-Fixing

The decision of the French Government to terminate as soon as practicable its experiment with wheat price-fixing, to which the Chamber of Deputies gave its assent on December 13 by a decisive vote, should be a matter of much interest to this country and to our neighbor on the north, where the disposition to try out price-fixing as a remedy for economic ills is as marked as it is elsewhere. In France as in this country agriculture is a center of the national interest, and the farmers have a strong representation in the Government. From the onset of the depression, and the decline in world wheat prices, efforts have been made to shelter the French wheat growers from its effects, and the scope of these efforts widened as the depression continued and the agricultural position became more difficult.

The law setting minimum wheat prices to French farmers dates back eighteen months. Thus the experience has been a short one, but it has been sufficient. The French Government has learned, as other governments making similar ventures have also learned, that price fixing offers no solution for depressed commodity markets, and its experiences add another valuable chapter to the record.

Lessons of the Experiment

Economic theory objects to price-fixing measures on the ground that by holding prices above their natural level they encourage production, disrupt trade, discourage consumption, perpetuate the surplus, and finally become unenforceable. Moreover, as long as they are in operation they constitute a subsidy to one group of the population, at the expense of other groups, and the cost is a burden on the national economy.

All of these effects have developed in the French experience. The surplus of wheat in France has grown unmanageable, and it is plain that the Government's measures, tending to maintain production and reduce consumption, have been an influence in accumulating it. In order to support the domestic market, it is necessary to export wheat at the expense of the national Treasury, which must make up to the farmer the difference between the domestic and the world price. The higher bread prices resulting from the program, and the costs to the Treasury, have provoked the resentment of the urban and industrial population.

Finally, a lesson has been learned as to difficulties of enforcement. A so-called "black" or bootleg market in wheat, trading at prices well below the official minimum, has been maintained despite all the efforts of the Govern-

ment. The situation has been described by some observers as an open defiance of the law by a considerable part of the milling industry, by farmers more anxious to sell their wheat than to hold it for the legal price, and by bakers. In the debate Premier Flandin admitted this situation. Meanwhile, however, the price of bread is fixed according to the official price of wheat, and unless there is "black" market for bread also the consumer gets no benefit from the illicit wheat trading, and the normal effects of a lower price in stimulating consumption are inoperative.

Since the initial price-fixing law was adopted three other laws and around one hundred decrees have been found necessary to supplement and strengthen it. Professor James E. Boyle of Cornell University, an outstanding authority on the grain trades, stated after an investigation made last Summer that the regulations applying to the wheat and milling trades, and doubtless necessary to the enforcement of the act, were so numerous and detailed that probably no lawyer in France was able to construe them correctly, although a leading attorney had issued a 715 page book devoted solely to explaining them. Under this regimentation the number of wheat dealers is said to have been cut in half. The milling business has become so difficult, especially for mills desiring to observe the price law, that some have closed.

How the Wheat Controls Spread

The history of the French wheat laws shows well how once started the habit of control tends to spread, each step leading to more drastic ones. Even before the depression, the protective policy was under way, in the form of a rapid increase in the tariff on imports of foreign wheat. The general tariff rate has been increased since January 1, 1927, from 19.6 cents per bushel to $1.71.

In 1929, when a crop of 337,000,000 bushels was raised, the first post-war crop to present a real surplus problem, resort was had for the first time to regulations limiting the use of foreign wheat in the manufacture of flour. Although French millers have normally used around 30 per cent of foreign hard wheats for mixing with their own soft wheats, they were limited at various times to 3 per cent, later 1 per cent, and finally (in the 1933 emergency) none. The quality of the bread has been affected by these limitations, and a naturally declining tendency in bread consumption has been accentuated.

In 1930 and 1931 unfavorable conditions reduced the crop, and the 1929 surplus was successfully moved. The accumulation of the present surplus began with the 1932 crop which turned out to be 334,000,000 bushels. From that year on the succession of measures to support the market, leading up to the price-fixing experiment, has been unbroken. For the first time the percentage of flour allowed to be extracted from wheat was limited, naturally adding to millers' production costs. The Government granted a bounty on exports of wheat, and finally it resorted to paying a subsidy to farmers who would hold their wheat, and to direct purchases; all without much effect. The price dropped from $1.87 per bushel, in Paris, in the middle of 1932, to around $1.15 at the beginning of 1933.

The carryover at the end of the 1932-33 season was large. Then the 1933 crop came to market, totaling 362,000,000 bushels, the largest since 1907, and 50,000,000 bushels in excess of the country's requirements. Confronted by this crop, the Government reduced the flour extraction rate to 65 per cent, compared with a normal of 76, and prohibited all use of foreign wheat in making bread flour. It established a bounty on denatured wheat fed to livestock, and increased the bounty on exports, finally as high as $1.63.

Most important of all, it passed the act fixing the minimum price to the farmer at 115 francs per quintal, equivalent to $2.09 per bushel at the present value of the franc. This price was increased by 2½ cents per month during the 1933-34 crop year, to allow for carrying charges and insure "orderly marketing"; and at the end of the season (August 1, 1934) the price in Paris was around $2.38. At the same time the surplus had mounted to 110,000,000 bushels, despite all the efforts to reduce it, and Argentine wheat was selling in Liverpool for around 75 cents.

The Present Situation

The 1934 crop has not relieved the situation. Estimated at 332,000,000 bushels, it also is substantially above requirements. The Government fixed the price of this crop at $1.96, and required millers to grind 65 per cent of old wheat with 35 per cent of new. Some wheat has been exported, and more has been sold for export. But with all the efforts the surplus is still estimated at from 90,000,000 to 110,000,000 bushels, private estimates being higher than the Government's figures. On the "black" market quotations are understood to have dropped below $1.50.

This was the situation confronting Premier Flandin when he took office in November. All the measures since 1929, and especially since 1932, had been offered only as temporary emergency measures, but the conclusion that the emergency might last as long as the measures lasted has impressed itself upon the country.

For details of the new wheat law we are dependent at this writing upon incomplete summaries, which state that the minimum price will be reduced from 108 to 97 francs per quintal ($1.96 to $1.76 per bushel) and will be

removed entirely in six months. The Government will eventually absorb the surplus, at a total cost estimated up to $125,000,000, financed by borrowings which will be serviced in part by taxes on producers and millers. M. Flandin told the Chamber that it was intended to export 36,000,000 bushels, of which over 20,000,000 will be denatured for livestock feed. A bounty of $1.18 on exports is provided. The remainder will be in part denatured, and in part stocked. It is proposed to reduce the price of bread by 12½ per cent or more, making it slightly lower than it was prior to enactment of the 1933 law. Penalties are placed upon any expansion of acreage. Planting of certain varieties of wheat, giving a high yield but of low quality, is forbidden.

Importance in the World Situation

To all those who have deplored the extreme nationalistic tendencies which have influenced the wheat policies of various countries, the new policy in France comes as an encouraging indication that a more moderate viewpoint is beginning to prevail. To be sure, no one expects that France, even after her surplus is absorbed, will soon modify her tariff or her restriction on wheat imports, or open her market freely to producers of cheaper or better wheats elsewhere. But an artificial inducement to wheat growing, leading to overproduction, has been withdrawn, and the policy is to discourage planting and prohibit expansion. French price-fixing has led to disturbance in the world situation, through the French export offerings, and the world wheat trade will finally be the gainer from its abandonment, which makes the production of continuous surpluses unlikely.

Any check to the expansion of wheat growing in the countries where the costs of growing it are high is a hopeful sign for better times in world trade. The subsidies and protective devices necessary to support this high-cost production, which have been redoubled during the depression, are a burden on the people who pay for them, and on the whole economic system. The wheat production of the European importing countries was increased, by means of these devices, by over 350,000,000 bushels between 1927 and 1933. Concurrently their consumption declined about 200,000,000. These shifts have thrown the wheat trade of the world into disorder, with effects familiar in this country, among others, and the disturbance has spread far beyond the wheat trade. It is unnecessary to expand upon this fact, in view of the loss of our own wheat export business, the low prices still being accepted by the countries which are exporting, and the consequent effects on business everywhere.

The foregoing considerations doubtless have had little to do with the change of policy by the French Government, and it is not reasonable to expect that they should have had. The policy of protecting the wheat growers was not adopted for the purpose of injuring other producers, but for what were deemed good and sufficient reasons connected with the national interest. However, the depression of the wheat industry has been due very greatly to the aggregate of the policies of many countries, each acting in their own interest, and the depression has reacted on all of them. The fact is that they have overlooked the advantages of trade.

It is idle to expect any stability in the wheat growing industry or in the world wheat trade as long as the production of wheat is governed not by calculable economic influences, such as the cost of growing it in various places and the quality produced, but by the incalculable political decisions of governmental bodies, based on uneconomic considerations. Nor is there reason to hope for more than a patchwork solution in the efforts to induce the cooperation of wheat growing countries on a basis of mutual sacrifice, each accepting production or export quotas; or in the vision of an internationally controlled wheat economy. The fallacy in the claims made for such an economy, even if it were practicable, is that its chief effect would be to preserve the high cost producer, for the curtailment would necessarily fall on the low cost exporting countries.

The Latest Upon Business Profits

In recent numbers of this publication we have given considerable space to authentic information regarding the profits of business and the distribution of the annual income of the nation among individuals. The purpose, as stated, has been to let the light of truth fall upon some of the falsehoods and misrepresentations regarding these subjects which are literally flooding the country, often sponsored, ignorantly or heedlessly, by persons of repute and position.

During the last month the Treasury has made public its final figures for the aggregate incomes, gross and net, of all corporations in the year 1932, with preliminary figures for the year 1933, and also its preliminary figures for the manufacturing corporations by themselves in 1933. This affords the data for extending our previous statements of corporation profits by including the latest available information. We give below the new figures for all corporations and for the manufacturing group, together with the final figures for the preceding years since 1929.

Gross and Net Income of All Corporations in the United States
(In Millions of Dollars)

	1930	1931	1932	1933*
Reporting Net Income:				
Gross Income	89,561	52,051	31,708	40,040
Net Income	6,429	3,683	2,153	2,506
Income Tax	712	399	286	354

Reporting No Net Income:				
Gross Income	46,501	55,464	49,376	28,796
Deficit	4,878	6,971	7,797	4,511
Consolidated:				
Gross Income	136,062	107,515	81,084	68,836
Net Income after Taxes	840	D-3,687	D-5,930	D-2,359

* Preliminary. D- Deficit.

Note 1: The year 1930 was the last in which the consolidated statement of all corporations showed a profit, this profit being 62/100 of 1% on gross income. Published reports for earnings in 1934 indicate improvement over 1933, but it is not certain that the gains have been sufficent to put the net result in black, and obviously the five years will show a deficit in the aggregate.

Note 2: Judging by past reports the apparent decline in gross income between 1932 and 1933 is exaggerated. When the final figures are available a year from now they will probably show several billion dollars added to the total of gross income, and probably some increase in the net deficit.

Gross and Net Income of All Manufacturing Corporations

(In Millions of Dollars)

	1930	1931	1932*	1933*
Reporting Net Income:				
Gross Income	38,804	20,974	10,514	17,921
Net Income	2,758	1,465	657	1,211
Income Tax	317	165	86	172
Reporting No Net Income:				
Gross Income	19,846	23,059	13,332	9,036
Deficit	1,640	2,288	2,103	966
Consolidated:				
Gross Income	58,650	44,033	23,846	26,957
Net Income after Tax	801	D-988	D-1,533	73
% Net on Sales	1.37	D-2.24	D-6.43	0.27

*Preliminary.

In our September (1934) number we gave figures from the Treasury statistics showing that the average profit of all corporations after taxes in the fourteen years 1919-1932, was 2.42 per cent of their consolidated turnover; or, omitting the years of net aggregate deficits (1921, 1931 and 1932), to eliminate their exceptional influence, the average for the remaining eleven years was 4.08 per cent of the volume of business handled; also that in the six years 1924-1929 the range was from 3.73 to 4.80 per cent, or an average of 4.35 per cent, upon the annual volume of business.

The same article also carried a table, compiled from the census statistics of the manufacturing industries by Professor F. C. Mills, of Columbia University, showing the increase in the physical volume of their production, in number of wage-earners employed and in output per wage-earner over the 30 years 1899-1929. The latter table was reproduced in our December number for further comment.

On November 23rd last The Associated Press of this country in a press dispatch from Stockholm summarized for its members the contents of a signed article by Professor Gustav Cassel of the University of Stockholm, which had appeared in the Svenska Dagbladet, a leading newspaper of Stockholm, the same presenting many of the figures used in the above-named article and drawing similar conclusions therefrom.

Professor Cassel is an economist of international distinction. Besides being a Professor of Economics in the University of Stockholm he has been a course lecturer at Oxford University and in the School of Economics of the University of London, and upon his visit to this country in 1928, delivered lecture courses in economics at Chicago and Columbia Universities. He visited Washington, D. C., in that year and was invited to appear before Congressional Committees. He is the author of several standard works on economics, and has been a leading figure in the international economic conferences held since the War. Believing that our readers will be interested in reading his discussion of the figures which they have already seen in these columns, we reproduce his article in full, as follows:

COLLAPSING DOGMAS

By Gustav Cassel

(Translation from the Svenska Dagbladet, Stockholm, Nov. 4, 1934)

For generations a number of false notions have been circulated regarding deep-seated defects, from which our social economy is supposed to suffer. Such notions have been fed, not only by agitation hostile to this social economy, but also by a mass of thoughtless meditations in the financial press. The false doctrine has been repeated so endlessly that it has gained a quite general belief. Neither has it been entirely easy to disprove it conclusively. To be sure it has been possible, on the basis of a general knowledge of social economy and its theoretical foundation, to demonstrate that the criticism has been ill-founded and, as a matter of fact, caused by very elementary misunderstandings. But for the most part there has been a lack of clear figures which could completely prove that the ideas here involved were quantitatively wholly erroneous.

In recent times, however, diverse statistical material has been brought out which permits us to throw a decidedly clear light on the main characteristic of the actual economy development. Especially have the very comprehensive economic statistics of the United States been of decided value in this respect.

During the thirty year period from 1899 to 1929 the American manufacturing industries increased the number of its workmen by about 3,500,000. In per cent this means an increase of almost two-thirds. The figure, to be sure, is not absolutely reliable, since the field covered by the statistics has been somewhat changed. It is most likely to be too low and in any event it seems fairly certain that relatively the increase has somewhat exceeded the increase in population during the same period. In general the manufacturing industries have therefore been able to provide employment for their proportional share of the increase in population. Naturally, there have been fluctuations and it has been especially noticeable that after an abnormally great increase there has followed a reduction. But the common notion that the manufacturing industry, thanks to a continuous rationalization and the measures connected with it to save labor power, must necessarily and continuously repel workingmen is shown to be unfounded so far as the United States is concerned. As a matter of fact, the manufacturing industries have been able to take on annually, on the average, considerably more than 100,000 workingmen a year, which certainly must be recognized as a decidedly admirable achievement.

The productive capacity has been estimated to have increased from 100 to 189.7 for each worker. A very decided increase in the productive efficiency has therefore been achieved. Together with the increase in the number of workers this gain in efficiency has brought about an increase in the total production, measured as "increase in value by manufacturing," from 100 to 311.4. The resulting production has therefore been more than trebled during the above period, and the manufacturing industry has thereby made a handsome contribution, not only to the necessary support of a rapidly increasing population, but also to an improvement in the standard of living.

Figured by the year the number of workers has increased by 1.67 per cent and the production per worker by 2.16 per cent. Consequently, there has been achieved an annual gain in production of 3.86 per cent. This figure probably corresponds very closely to the general speed of progress of the American social economy, but exceeds very decidedly the average rate of progress in the Occidental countries which is usually estimated at three per cent.

We therefore find that a typical capitalistic social economy has not at all, as claimed by current notions, lost its efficiency because of lack of "planned economy," whether in ability to produce or to employ labor power.

Another criticism which is usually aimed at the capitalistic order of society and particularly against the development in the United States is that the large enterprises amass an unreasonable profit at the expense of the public, with the result that the purchasing power of the latter decreased and that the enterprises cannot find any other use for their profits than to increase still more their productive capacity, for which an adequate market is lacking. Statistics show that after payment of taxes the net income of the combined corporations in the United States constitutes a very small portion of the companies' total gross sales revenue. The percentage for the years 1922-29 hovers around four per cent and in general does not much exceed this figure. It is hard to see how the companies could be satisfied with a lower average rate of profits on what they have to sell. That it has been pressed down as low as that depends naturally on the sharp competition which always makes it necessary for some enterprises to sell their products below the actual costs of production. One must, of course, be careful when drawing conclusions from such average figures. But they no doubt do show with certainty that there is no foundation for the current notions that the corporation profits are so unreasonably large that they must cause a thorough upset of the entire social economy.

During the boom period from 1924 to 1929 the total sales figure or gross income of the corporations increased by about six per cent a year, which is a handsome but according to American conditions certainly not at all an unusually sharp increase. In the meanwhile the net profits varied from 3.73 per cent and 4.80 per cent of the total sales. These figures are quite sufficient to upset the doctrine continuously repeated throughout the world that the violent crisis in the United States was due to an unnatural expansion of industry and a consequently enormous collection of profits. The cold figures now at hand show that there is not the slightest foundation for this whole doctrine, which during five years has served throughout the world as the foundation for thoroughly erroneous explanations of the crisis and for the most unjustified attacks on our entire social economy.

The picture statistics give us of the development of American business enterprises shows in general a decided advance where the "capitalistically" organized enterprises, that is to say the stock companies, have brought down their profits by an exceptionally strong competition with each other to a minimum and thereby have transferred to the great mass of consumers the preponderant share of the fruits of progress.

With the crisis of 1929 there appears a very serious break in the development. But this break is due essentially to the bad conditions in the world economy, which go back to the war and the war debts, and, above all, to a complete mismanagement of the world's monetary affairs. **The actual facts give not the slightest support to the contention that the world crisis reveals the worthlessness of the capitalistic system of production. It is also a mistake to interpret the crisis as a proof that production as a whole had previously been speeded up too much. The only possible solution of the great social problems is that production be permitted to develop at the pace it followed before the world crisis. By cutting down production, stopping the exchange of goods and putting enterprise under guardians we shall never create any prosperity.** Despite the enormous progress attained during the present century, the world supply of goods at the outbreak of the crisis was entirely too scanty to enable the peoples to live at what is nowadays considered to be a decently human standard. We must again begin a strong increase in production, preferably at the pace set by America before the crisis, and we must steadily go ahead along that line in the assurance that this is our only possibility to fill even approximately the demand of the future for prosperity.

Professor Cassel's Argument

In the last paragraph of his article, in touching upon the cause of the depression, Professor Cassel again repeats his oft-stated opinion that it was the unbalanced state of trade and of international capital transactions (all resulting from the Great War) which broke down the gold standard and involved the world in monetary confusion. We have repeatedly emphasized that these disorders did not arise from the normal operations of the economic system, but from the extraordinary demands upon the system resulting from the War. We have heretofore quoted the Professor's opinion that the disruption of price-relations between the crude primary products of rural populations, who comprise more than one-half of the world's population, and the products of the more highly organized industries and services (caused by the War), had "put the entire world economy out of balance." This is the theory held by Secretary Wallace and made the basis of the policies of the Department of Agriculture.

Also what he says about the policy of spreading work, reducing the hours of productive operations and restricting improvements in industry, has the approval of all economic authorities, who are practically agreed that under normal conditions the products of industry will pay for each other in trade without limit, if produced and priced in an orderly manner under the simple and impartial guidance of the law of supply and demand.

Professor Cassel expresses his views with a simplicity, clarity and vigor of language which attest to his familiarity with the subject. They have the merit and weight which derive from being general in application and based wholly upon the economic principles involved, without any relation to American partisan politics.

Changing Industrial Conditions, 1914-1934

The National Bureau of Economic Research, Inc., issued its final Bulletin for 1934, (No. 53) entitled "Changes in Prices, Manufacturing Costs and Industrial Productivity, 1929-1934."* The author is Professor Frederick C. Mills, of Columbia University, whose work "Economic Tendencies," we have heretofore referred to as the most comprehensive and discerning review of the 30-year period, 1899-1929. Professor Mills is a competent student

* These bulletins upon timely economic subjects are issued, five in each year, at 25 cents each, or $1 for all. The Bureau is a non-profit organization for impartial research in economic, social and industrial science. Address: 1819 Broadway, New York, N. Y.

of industry in all its relations. This bulletin gives an instructive review of the confusion in economic relations since 1929. It begins with a general statement which is in itself an explanation of the depression:

> Every major business recession disrupts existing ties among the elements of the economic system. * * * Such balance as may have existed between the incomes of consumers and the aggregate value of goods offered for sale is dislocated. Established relations between production costs and final selling prices are radically altered in a period of sharp price decline. The host of price relations that condition the movements of goods along the channels of trade are subject to shifting and distortion. * *
>
> The wide inequalities of price changes occurring during the last five years have been at once manifestations of profound disturbances in the physical conditions of production and distribution and obstacles to the resumption of normal activity.

The simplest method of comparing statistical information of various but related kinds over a term of years is by the use of index numbers, 100 representing the figures of the base date and the figures of subsequent dates representing percentages of 100. Table No. 1 of this bulletin, composed of index numbers, affords a picture of the confusion in prices, wages and earnings, living costs, etc. from July, 1929 to October, 1934, as compiled by Professor Mills from government tables.

Table I—Index Numbers Defining Changes in Various Elements of the Price Structure of the United States, and in Related Factors, July, 1929, to October, 1934

Economic element[1]	July 1929	Feb. 1933	July 1933	Oct. 1933	Oct. 1934
Wholesale prices	100	62	71	74	79
Cost of living of industrial workers	100	74	77	80	82
Retail food prices	100	57	66	67	73
Retail prices of clothing and house-furnishings	100*	59	64	74	74
Prices received by farmers	100	37	56	53	68
Prices paid by farmers	100	66	70	76	82
Hourly earnings, manufacturing labor	100	77	76	95	102†
Per capita earnings, employed mfg. labor	100	65	70	74	76
Av. per-unit purch. power of farm prod.[2]	100	57	81	70	82
Real per capita earnings, employed mfg. labor[3]	100	88	91	93	94

*October, 1929

†September, 1934

[1]Sources and descriptions of these index numbers appear in the Appendix Note of the Bureau Bulletin.

[2]Percentage relation of index of average prices received by farmers to index of average prices paid by farmers for commodities used in production and in family maintenance.

[3]Percentage relation of index of average weekly earnings of manufacturing employees to index of cost of living of industrial workers.

The above table serves to illustrate the disorder in economic relations since 1929, but we think a more complete understanding of the disorder is obtainable by extending the study over the entire period of the Great Disturbance, which began in 1914. The Bureau has covered the period of rising prices in previous bulletins, and to make the story continuous we give herewith a companion table, corresponding so far as information is available, but based upon pre-war conditions as 100. It shows the rise to 1920-1929, and the general decline to 1934. Except as shown by foot-notes, the sources of information are the same as given for the table above. We have changed the order of the items to bring the more closely related ones together, and have added railroad freight earnings and wages, because of the relation of transportation costs to all of the exchanges; also building costs and interest rates, as important elements in the business system. Our table follows:

INDEX NUMBERS DEFINING ECONOMIC CHANGES

	Pre-war	July 1917	July 1920	July 1921	July 1929	Oct. 1934
1. Wholesale Prices						
(a) General index	100	176	238	134	140	110
(b) Raw materials	100	184	241	122	144	105
(c) Finished prod.	100	165	227	143	141	114
2. Cost of Living of Industrial Workers						
(a) General av.	100	128	199	164	161	131
(b) Clothing	100	143	266	164	166	132
(c) Housing*	100	105	158	169	159	115
(d) Furnishings ¶	100	—	281	216	191	161
3. Retail Food Prices	100	146	219	148	159	116
4. Earnings of Employed Mfg. Labor						
(a) Hourly money earnings	100	—	245*	205*	239*	240
(b) Weekly money earnings	100	—	236*	181*	226*	158
(c) Hourly real earnings	100	—	125*	125*	147*	184
(d) Weekly real earnings	100	—	121*	110*	139*	121
5. Position of Farmers						
(a) Prices received	100	175†	211†	125†	148	102
(b) Prices paid	100	149†	201†	152†	152	126
(c) Avg. per unit purch. power of farm prod.	100	117†	105†	82†	97	81
6. Rail Transportation						
(a) Freight revenue per ton-mile†	100	99	145	176	148	137
(b) Hrly. wage rates of r.r. employes	100	120†	268‡	242	245	241**
7. Building						
(a) Build. mat. costs	100	166	267	166	171	150
(b) Build. wages	100	109	189	180	233	204
8. Interest Rates (Actual)						
(a) Commercial paper	4.83	4.68	7.84	6.28	6.00	1.00
(b) Yield on Municip. bonds	4.22	4.29	5.25	5.34	4.28	3.69
(c) Yield on prime corp. bonds	4.78	4.98	6.40	6.18	4.89	4.77
9. Costs of Government †						
(a) Federal, state and local expenditures	100	—	—	340‖	447	501‡‡
(b) Federal, state and local tax collect.	100	—	341§	404	446	503‡‡

† Annual figures ** September, 1934 ‖ 1923

* Third quarter ‡ August § 1919

¶ Bureau of Labor Index—all figures as of middle of the year. ‡‡ 1933 estimate.

Note: The pre-war base is 1913, 1914, July 1914, Dec. 1914, 1915 or the five year average ending with one of these years.

The two tables together afford a picture of the violent changes in prices and trade relations since 1914 and should enable any one to understand why goods have not been flowing freely between the several groups of the economic system since the decline of prices began in 1929. They also show the effects of the slump of prices from 1920 to 1921. The two tables are related through the second table's numbers for July 1929, which not only represent the percentage-changes from the pre-war base, but represent the base (100) of the first table.

Under the influence of the war, with the demand for man-power and the disruptions of trade, the general price-level rose rapidly, farm products leading, but this rise culminated in 1920 and at no time since about the middle of that year has the average purchasing power of farm products been as high as at the pre-war base. The pressure for farm relief has been continuous at Washington since 1921, and the loss of farm purchasing power has affected employment in the other industries since 1920. That loss of purchasing power has been aggravated by the relatively high prices of what farmers have had to buy, as shown by both tables.

The most notable feature of the tables is the small advance in prices of finished goods, as given by the Bureau of Labor tables, in 1934 over 1914 (14 per cent), in view of the rise in hourly wage-rates in manufacturing (140 per cent) as reported by the same authority, and a rise also in raw materials, transportation costs and an increase of taxation. Almost the only means of overcoming these rising costs has been the increasing efficiency of the industries, referred to further on. A minor factor has been the absence of any average profit to the manufacturing industries since 1930.

The effects of this increasing efficiency are seen also in the fact that the rise of the cost of living (31 per cent) and the rise of the ton-mile transportation charge (44 per cent) are both much less than the rise of wage-rates entering into those costs.

On the other hand, although the prices of farm products and raw materials rose faster than wages in the war period, they were the first to give way when the pressure of the war and boom times slackened, and the disparity reached its extreme stage in 1932 and early months of 1933. The policy of the urban industries in spreading work, shortening the work-week and raising hourly wages has had the effect of increasing industrial costs and prices and also the cost of living. The employed workers whose wages were raised had this compensation for the rise of living costs, but the mass of people whose incomes were not increased evidently were worse off by the policy. Summing up the effects, it must be said that all such gains to producers are at the expense of consumers, and that wherever trade relations are unbalanced consumption will decline.

The difference between "hourly earnings of employed manufacturing labor," "per capita earnings, employed manufacturing labor" and "real per capita earnings employed manufacturing labor," as appearing in the Bureau table and similar figures in the second table, show the effects of the policy of spreading work, shortening the work-week and raising hourly wages. Obviously it is the wage for time actually worked which enters into industrial costs and the cost of living, while the lower "per capita" or "weekly" earnings reflect the idle time which has been lost to the workers. Notwithstanding the great rise of hourly wage-rates from 1914 to 1934, the net result in "real weekly earnings" (wages measured by their purchasing power over costs of living) show an increase of only 21 per cent, and this gain is offset by unemployment. What has become of the gains which should have resulted to the workers from the increasing efficiency of the industries? The answer is—lost in the wastes of disorder!

The above illustrates the statement made herein last month, that no group in the economic system can gain anything by raising its charges *above* fair reciprocal relations with the other groups with which it is trading. To do so, disturbs the equilibrium which is necessary to complete employment and a full volume of trade. On the other hand, to raise the compensation of a group which is *below* the reciprocal basis of trade restores the normal equilibrium and increases employment and consumption, with benefits to all. In other words, there is a just balance in trade relations which yields the best possible results for all. This is the significance of "economic law".

Reviewing the various disparities appearing in table No. 1, Professor Mills says:

> Each of these major differences represents a host of individual cleavages, breaks in a multitude of producing and trading relations. The net result is to check normal activity until readjustment to new relations can be effected, or until working approximations to old relations may be established.

He finds that price relations between the major groups have improved decidedly since February, 1933, which obviously is the statistical situation. It is only prudent to take account of the abnormally temporary and uncertain influences which have contributed to this improvement, and which make it difficult to appraise the permanent gain in group relations. Among these are short crops, Government subsidies, relief expenditures, monetary devaluation, budgetary deficits, uneconomical employment forced upon private industry, etc. These are temporary factors which eventually must disappear. Lasting prosperity must be based upon normal group relations and sound economy throughout public and private affairs.

The Manufacturing Industries

Discussing the manufacturing industries the author says:

> The trading relations of manufacturing industries with other major producing groups have been demoralized by the price inequalities developing during the recession, and persisting thereafter. In following the fortunes of these industries during depression and recovery we shall be dealing with matters lying near the heart of our current troubles.

He touches upon another interesting point when he notes that "the reduction in the volume of manufactured goods was considerably greater than the net decline in average selling prices." This statement might be turned around to read, "The smaller the decline in prices the greater the decline in sales," something not difficult to understand. All of the industries which maintained their prices close to the 1929 level lost heavily in volume of business, for the evident reason that the other groups, whose prices had fallen, were unable to maintain their former volume of purchases at the same prices—another demonstration of the law of the equilibrium in economic relations. Economic principles are founded in equity, and unless economic relations are equitable (truly reciprocal) the volume of business declines. The author's comment upon this point is that "declining sales and reduced production were necessary accompaniments of the retarded drop in the selling prices of manufactured goods."

A great deal of erroneous criticism was directed at employers while prices were falling, for their efforts to reduce costs and prices in order to maintain volume of business and employment. They were constantly urged to maintain both production and wages in the face of declining sales, and the only way this could have been done was by manufacturing for stock. Since on the average the manufacturing industries must pay out more than 90 per cent of the selling value of their products in operating costs, there is a very definite limit to that policy. It is quite apparent now that if this policy had been adopted early in the depression, and to the extent of borrowing money for the purpose, it might easily have bankrupted every industry in the country, which would have made the depression even more disastrous than it has been.

A Way Out of the Depression

The most encouraging showing of the review is the increasing productivity of labor, not only prior to 1929 but since that year. Of this Professor Mills says:

> The decade 1919-1929 witnessed one of the greatest advances ever recorded in industrial productivity in American manufacturing industries. Output per worker employed increased no less than 41 per cent. The significance of this figure may be brought home more vividly if we realize that it means that in 1929, 71 men, working with the improved equipment then available, could produce the volume of goods for which 100 men were required in 1919. * * *
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> From 1929 to 1933 there appears to have been an advance of approximately 15 per cent in output per man-hour, this on top of a gain of 41 per cent in output per capita during the preceding ten years. This increase in productivity and a parallel reduction in hourly wage rates during the stage of business recession have made possible a steady reduction in labor cost per unit of manufactured product. The decline in labor cost per unit of product probably exceeded 25 per cent from 1929 to 1933. Material costs per unit have declined in greater percentage, and the decline of overhead costs plus profits approximates that of labor costs.

The General Conclusion

Everything in this review supports the opinion that the state of depression and unemployment is a result of disorder in trade relations (primarily caused by the Great War), which has created a state of blockade in the movement of products into consumption. The various goods and services are not priced to each other in accustomed relations. The shortest way out of this situation would be by equitable readjustments, raising prices and other compensations which are relatively low and lowering such as are relatively high, the effect of which surely would be to increase trade, consumption and employment. All would benefit thereby and the effects would be another demonstration of "economic law."

Moreover, such readjustments are assisted by improvements in methods of production which enable both industrial costs and living costs to be lowered without reducing wage-rates, thus increasing the purchasing power of all incomes. This means that all restraints upon the installation of improved machinery should be abandoned, which would revive the capital goods industries, wherein the greatest unemployment exists. There is no reason to doubt that the capital goods industries will revive when the demand for consumers' goods recovers normal proportions. Probably one-half of the machine equipment of the industries ought to be replaced now and would be promptly if there was assurance of a rapidly increasing volume of trade.

The gain of 15 per cent in man-hour productivity in the manufacturing industries in the four years 1929 to 1933 has been accomplished by the initiative, enterprise, investments and labors of proprietors, managers, inventors, research workers, and others engaged in these industries, working primarily to increase the efficiency of the various organizations to which they belong, but all contributing to this beneficent result. It is a better showing than the average over the 30-year period, 1899-1929, given in these columns last month. Moreover, improvements have been made in the methods of producing the raw materials, and in the methods of transportation and merchandising by which these products are distributed to consumers. All of such gains afford a margin for the readjustments which are now required to restore the normal equilibrium of the system.

Indeed, it is truly remarkable (as appears from the commodity prices of the tables) how far the economic system has progressed in the task of overcoming the derangements caused by the war, and this with so little conscious cooperation between its parts and with enormous difficulties arising from outside of itself, as illustrated by the French legislation affecting wheat, described in a preceding article.

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